No. 84-233

IN THE

Supreme Court of the United States

OCTOBER TERM, 1984

PHILLIPS PETROLEUM COMPANY,
Petitioner,

v.

IRL SHUTTS and ROBERT ANDERSON and BETTY ANDERSON, individually and as representatives of all producers and royalty owners to whom Phillips Petroleum Company made payment of suspended proceeds of royalties pursuant to Federal Power Commission Opinion Nos. 699, 699H, 749, 749C, 770 and 770A,
Respondents.

On Writ of Certiorari to the Supreme Court of the State of Kansas

REPLY OF PHILLIPS PETROLEUM COMPANY

ARTHUR R. MILLER
1545 Massachusetts Avenue
Cambridge, MA 02138

JOSEPH W. KENNEDY *
ROBERT W. COYKENDALL
MORRIS, LAING, EVANS, BROCK & KENNEDY, CHARTERED
Fourth Floor, 200 West Douglas
Wichita, KS 67202
316-262-2671

WILLIAM G. PAUL
C. J. ROBERTS
T. L. CUBBAGE, II
Phillips Petroleum Company
Legal Division
1256 Adams Building
Bartlesville, OK 74004

* Counsel of Record
Attorneys for Petitioner

Date: February 15, 1985

WILSON - EPES PRINTING CO., INC. - 789-0096 - WASHINGTON, D.C. 20001

TABLE OF CONTENTS

TABLE OF CONTENTS—Continued

TABLE OF AUTHORITIES

TABLE OF AUTHORITIES—Continued

TABLE OF AUTHORITIES—Continued

REPLY OF PHILLIPS PETROLEUM COMPANY[1]

I. PHILLIPS HAS STANDING TO QUESTION THE APPROPRIATENESS OF KANSAS ASSERTING JURISDICTION OVER UNNAMED NONRESIDENT CLASS MEMBERS WHO HAVE NO AFFILIATION WITH THE FORUM

Contrary to the respondents' assertion, Phillips clearly has the requisite standing to challenge the Kansas court's assumption of jurisdiction over those class members who have no contacts with Kansas. By allowing an action that legitimately could be brought only on behalf of a few hundred people to be bloated to include 28,100 class members, the court below has exposed Phillips to a liability far beyond its power. This amounts to a direct violation of defendant's rights of such magnitude that Phillips has the unquestionable standing to challenge it before this Court. Independently, the circumstances of this case allow Phillips to advocate the rights of the absent class members.

A litigant certainly has the right to challenge the propriety of the parties arrayed against it. Thousands of persons beyond the jurisdictional reach of the court below have been swept up in this action by that court and have been awarded judgment against Phillips. The burden of litigating these claims and the dimension of the resulting liability Phillips faces provides Phillips with a "personal stake" in the outcome of the controversy. *Baker v. Carr*, 369 U.S. 186, 204 (1962).[2] This personal stake resulting from the harm caused by the Kansas court's actions gives Phillips the Article III

---

[1] Petitioner's statement pursuant to Supreme Court Rule 28.1 is set forth at Pet. App. p. A68.

[2] The "personal stake" that Phillips has in this litigation should be contrasted with the "personal stake" a plaintiff, whose claim has been rendered moot, possesses in seeking reversal of a denial of class certification. That plaintiff, whose personal interests will be affected indirectly at best, has standing to litigate that case. *United States Parole Commission v. Geraghty*, 445 U.S. 388 (1980).

standing that enables it to contest Kansas' transgression of the Constitution's limits on state court jurisdiction and to clarify the extent of the judgment against it.[3] *Duke Power Co. v. Carolina Environmental Study Group*, 438 U.S. 59 (1978).

In *Hanson v. Denckla*, 357 U.S. 235 (1958), this Court went further and held that a defendant had the right to question a state's jurisdiction over a trustee who was a mere stakeholder, although an indispensable party under state law. Standing, in this context, is not premised on a defendant's concern for the rights of the absent plaintiffs, as the respondents erroneously suggest, but on a defendant's legitimate concern for its own rights. As the Court has said, standing exists whenever "any defendant affected by the court's judgment has that 'direct and substantial personal interest in the outcome' that is necessary to challenge whether that jurisdiction was in fact acquired." *Id.* at 245, *quoting*, *Chicago v. Atchison, T. & S.F.R. Co.*, 357 U.S. 77, 83 (1958).

A nonresident class member is undoubtedly an indispensable party to the adjudication of his own claim against Phillips[4] making the existence of a constitutionally sufficient jurisdictional base over him imperative.[5]

[3] If Phillips cannot challenge the court's jurisdiction over the nonresident class members, it never will have its day in court on the legitimacy of the resulting judgment inasmuch as no successful class member ever will raise the issue collaterally. This creates a lack of mutuality because a member of a losing class has such an incentive. Respondents' analogy to one-way collateral estoppel is false because in that situation the party against whom the estoppel is to run has had a full and fair opportunity on the issue in the first action.

[4] With respect to a nonresident's cause of action against Phillips, each nonresident has "not only . . . an interest in the controversy, but an interest of such a nature that a final decree cannot be made without . . . affecting that interest . . . ." *Shields v. Barrow*, 58 U.S. (17 How.) 130, 139 (1854).

[5] This concept has been incorporated into the Federal Rules of Civil Procedure. A defendant can move to dismiss for failure to join an indispensable party. Fed. R. Civ. P. 12(b)(7). The motion

Indeed, a judgment's effect on absent indispensable parties even can be questioned by a court on its own initiative. See *Provident Tradesmens Bank & Trust Co. v. Patterson*, 390 U.S. 102, 111 (1968). Phillips plainly possesses a cognizable interest in whether the Kansas court can encompass nonresidents within its judgment.

Phillips is doing nothing more than raising traditional defenses of improper joinder of parties and improper class definition. The Kansas class action statute gives Phillips the right to litigate these questions. That statute requires the Kansas courts to find that a class action is superior to other means of resolving the controversy by considering "the interest of members of the class in prosecuting or defending separate actions . . ." and "the appropriate place for maintaining, and the procedural measures which may be needed in conducting a class action." Kan. Stat. Ann. § 60-223(b)(3)(A), (C).[6]

Not only can Phillips assert the constitutional violation of its own rights, Phillips also has standing to assert the liberty interests of nonresident class members. This Court has recognized that a defendant may advance the rights of third parties defensively as a bar to a judgment without encountering an Article III standing problem. *Warth v. Seldin*, 422 U.S. 490, 500 n.12 (1975). Any restraints applicable to standing to assert jus tertii arise not from the Constitution, but rather from the Court's own "rules of self governance." This Court repeatedly has upheld the standing of a party to assert the rights of others so as to avoid a harmful judicial determina-

even can be made by a defendant "seeking vicariously to protect the absent person against a prejudicial judgment . . . ." 1966 Advisory Committee Notes to Fed. R. Civ. P. 19, reprinted in 12 C. Wright & A. Miller, *Federal Practice and Procedure* 404 (1973). Kansas has an identical rule. Kan. Stat. Ann. § 60-212(b)(7).

[6] This statute is patterned after Federal Rule 23. That rule, like the Kansas statute, contemplates that a court will make the class action determination "with the aid of the parties." 1966 Advisory Committee Notes to Rule 23, reprinted in 12 C. Wright & A. Miller, *Federal Practice and Procedure* 416 (1973).

tion. The "rule of practice" limiting a party's ability to present another's interest is overborn "where there are weighty countervailing policies . . . ." *United States v. Raines*, 362 U.S. 17, 22 (1960).

The liberty interests of the nonresidents not to have their claims adjudicated by Kansas will be lost if the Court fails to consider this issue. It is absurd to believe that the right of absent class members to avoid an improper forum will be presented by the named class representatives or their counsel whose interests lie in maximizing the class's size. See *Deposit Guaranty National Bank v. Roper*, 445 U.S. 326, 338 n.9 (1980). The *only* party with an incentive to test the court's jurisdiction is the defendant.

There is no conflict between Phillips' interest in avoiding the assertion of jurisdiction by Kansas over the national class and the nonresidents' liberty interests in avoiding having their claims decided by the Kansas court.[7] Phillips certainly has enough incentive to advocate these absent class members' rights to insure that the constitutional question will be presented vigorously and fully for the Court's resolution. See *Craig v. Boren*, 429 U.S. 190, 194 (1976). The liability imposed on Phillips in the Kansas courts and its efforts throughout this controversy to litigate the jurisdiction question provides a basis for allowing Phillips to continue to advocate jus tertii before this Court. *Eisenstadt v. Baird*, 405 U.S. 438 (1971).

Moreover, a statute may grant a party the necessary basis for asserting the rights of third parties. *E.g.*,

[7] The respondents' position concerning standing seems to make it depend upon the outcome of the lawsuit. The respondents' argument that Phillips is without standing is premised on the idea that the class is completely victorious in this lawsuit. But a proper application of choice of law in this case could result in a portion of the class losing. This places the interests of Phillips, in avoiding the burden of litigation in Kansas, and the economic interests as well as the liberty interests of these class members in avoiding an adverse result in a forum with which the nonresident has no connection, in complete accord.

Warth v. Seldin, supra at 509; *Doe v. Bolton*, 410 U.S. 179, 188 (1979); *Griswold v. Connecticut*, 381 U.S. 479, 481 (1965). As discussed earlier, the Kansas class action statute contemplates that issues of joinder, jurisdictional location and other matters will be raised and litigated by defendants. *E.g., General Telephone Co. of Southwest v. Falcon*, 457 U.S. 147 (1982). Kansas repeatedly has permitted defendants to question the make up of the class arrayed against them by raising due process concerns. *E.g., Wortman v. Sun Oil Co.*, 236 Kan. 266, 690 P.2d 385 (1984); *Shutts v. Phillips Petroleum Co.*, 222 Kan. 527, 567 P.2d 1292 (1977) (*Shutts I*); *Gray v. Amoco Production Co.*, 1 Kan. App. 2d 338, 564 P.2d 579 (1977). The Kansas Supreme Court's apparent recognition of Phillips' right under Kansas law to raise these questions is binding on this Court to the extent it is based on Kansas law. See *O'Brien v. Skinner*, 414 U.S. 524, 531 (1974).

The jurisdictional issue now before this Court has been decided inconsistently by a number of state courts. Usually, the defendants assert the rights of the nonresident class members to limit the size of the class. *E.g., Miner v. Gillette Co.*, 87 Ill. 247, 428 N.E.2d 478 (1981), *cert. granted*, 456 U.S. 914, *cert. dismissed*, 459 U.S. 86 (1982); *Schlosser v. Allis-Chalmers Corp.*, 86 Wis.2d 226, 271 N.W.2d 879 (1978); *Feldman v. Bates Manufacturing Co., Inc.*, 143 N.J. Super. 84, 362 A.2d 1177 (App. Div. 1976). Unless this Court resolves this issue, confusion and uncertainty regarding both the jurisdictional power of state courts and the status of "national" class action judgments in other states will continue.[8] The pressing need to stabilize this burgeoning

[8] Resolution of this question will have a significant impact on a wide range of pending cases, including class actions in federal courts. *E.g., Jones v. Medtronic, Inc.*, Case No. CV-84-L-24555 (N.D. Ala.); *Linkous v. Medtronic, Inc.*, Case No. 84-1909 (E.D. Pa.) (conflicting nationwide product liability class actions). See also *In re Asbestos School Litigation*, Case No. 83-0268 (E.D. Pa.) (issue of jurisdiction over national diversity class raised and now on appeal to Third Circuit).

area of state court litigation, as well as the fact that it undoubtedly will be pressed on this Court in future cases, indicates that invoking the Court's limitations on the "assertion of jus tertii would 'serve no functional purpose.'" *City of Revere v. Massachusetts General Hospital*, 463 U.S. 239 (1983), *quoting*, *Craig v. Boren*, *supra* at 194.

In the past, this Court has permitted the use of third party standing when a state court has considered the issues raised. In this situation, a decision "to forego consideration of the constitutional merits in order to await the initiation of a new challenge . . . by injured third parties would be impermissibly to foster repetitive and time-consuming litigation under the guise of caution and prudence." *Craig v. Boren*, *supra* at 193-94. See also *City of Revere v. Massachusetts General Hospital*, *supra*.

II. RESPONDENTS HAVE OFFERED NO JUSTIFICATION FOR DEVIATING FROM THE CONSTITUTIONAL LIMITS ON STATE COURT JURISDICTION ESTABLISHED BY THIS COURT

A. The Purported Differences Between an Unnamed Nonresident Plaintiff Class Member And A Nonresident Defendant Are Illusory And Not Constitutionally Significant

Respondents apparently concede that the Kansas court had no constitutional basis under *International Shoe* for asserting jurisdiction over the nonresident class members since they seek to uphold the decision below solely on the ground that an unnamed nonresident plaintiff class member occupies a "significantly different position" than a nonresident defendant. Three primary differences are mentioned. First, if a nonresident defendant fails to appear, he is faced with a default judgment. Second, a nonresident defendant faces the possibility that a coercive judgment will be enforced against him. Third, a nonresident defendant must obtain counsel in the forum. Respondents Brief p. 16. Phillips submits that these differences have no substance and do not justify ignoring

this Court's decisions establishing limits on state court jurisdiction. There simply is no constitutional basis for treating the claims possessed by class plaintiffs as a property right that is subject to any lesser protection than any other property. *Logan v. Zimmerman Brush Co.*, 455 U.S. 422, 428 (1982).

A nonresident defendant not subject to a court's jurisdiction does not risk having a *binding* default judgment entered against him. A nonappearing defendant always can raise the lack of jurisdiction as a collateral attack on the judgment. *Chicago Life Ins. Co. v. Cherry*, 244 U.S. 25, 30 (1917). Ironically, under the respondents' view, the nonresident class member who has no contacts with Kansas would be in a worse position than a nonappearing defendant because he could be bound by the Kansas courts even if he took no action with respect to the Kansas litigation.

Nor does the fact that class plaintiffs may not face coercive judgments provide a meaningful distinction. This Court never has limited due process protections only to those defendants who face "coercive court orders." Mere stakeholder defendants are protected, *Hanson v. Denckla*, *supra*, as well as defendants faced with the extinction of personal claims, *Estin v. Estin*, 334 U.S. 541 (1948), and defendants threatened with no direct economic impact. *Rush v. Savchuk*, 444 U.S. 320, 331 n.20 (1980). Even assuming that nonresident class members are not subject to coercive orders, an extremely dubious assumption,[9] there is no basis for exempting unnamed nonresident class

---

[9] Respondents are incorrect in asserting that Kansas would not allow counterclaims against absent class members. Kansas has permitted claims by defendants in a class action to be offset against the amount of the final award. *Waechter v. Amoco Production Co.*, 217 Kan. 489, 537 P.2d 228 (1975); *Hemley v. Ashland Oil, Inc.*, 1 Kan. App. 2d 532, 571 P.2d 345 (1977). It is undecided whether a claim by a defendant that exceeds an award to a class plaintiff could result in a Kansas court entering a judgment against a plaintiff class member.

members from due process protections simply because they are labeled plaintiffs.

Finally, the claim that a nonresident defendant "invariably" is required to obtain counsel not only is incorrect factually, but also cannot support the constitutional distinction fabricated by the respondents. Since the right of a defendant to attack a default judgment collaterally is not impaired by a failure to appear, forum counsel is not always required. Moreover, the respondents' notion that the nonresident class members have not "retained" counsel ignores reality. Class certification is not possible unless the class is represented adequately, which universally is understood to mean having adequate counsel. Furthermore, in Kansas, nonresident plaintiffs have been compelled to compensate class counsel in an amount equal to between one-fourth and one-third of the class recovery. See Comment, *The Kansas Class Action Device*, 31 Kan. L. Rev. 305, 315-16 (1983). The fact that class members are provided with an attorney complete with a contingent fee arrangement does not justify a lesser constitutional standard of scrutiny.

B. Mere Notice, Representation And A Right To Opt-Out Cannot Cure The Total Absence Of A Constitutional Basis For Jurisdiction

Respondents devote a considerable portion of their brief to the argument that the class action procedures can be substituted for this Court's recognized limits on state court jurisdiction. Respondents refuse to recognize that the class action procedure is only a procedural device to achieve some litigation efficiency and economy. It should not be glorified above all else. The special procedural safeguards imposed on class actions are designed to compensate for the fact that it is a representative action that deprives the individual class member of his right to a formal day in court. These procedures are not a substitute for the constitutional requirement that there exist a basis for jurisdiction.

Traditionally, jurisdiction over a person has been analized in terms of two different elements—basis and process. Under this analysis:

> A court cannot exercise personal jurisdiction over a party unless a proper basis exists. Basis refers to the relationship between the party and the territory of the state from which the court's authority derives.

R. Casad, *Jurisdiction in Civil Actions* ¶ 1.01[2][a] (1983). This principle has been recognized in every decision of this Court since *Pennoyer v. Neff*, 95 U.S. 714 (1878). The approach of the court below and the respondents abandons any need for a basis on which to predicate the exercise of jurisdiction.[10] It allows mere notice to the class members and representation to bind nonresidents, even in the absence of any relationship between the forum and the nonresident, and in the face of this Court's unequivocal pronouncement that "all assertions of state court jurisdiction must be evaluated according to the standard set forth in *International Shoe* and its progeny." *Shaffer v. Heitner*, 433 U.S. 186, 212 (1977).

The respondents' approach would permit Kansas to concoct a procedure for binding nonresidents having absolutely no connection to the forum. All that is necessary is to send nonresidents a letter informing them that a

---

[10] This attitude is most obvious in the amicus brief of Public Citizen. Analyzing this case only in terms of the procedural safeguards case of *Mathews v. Eldridge*, 424 U.S. 319 (1976), the Public Citizen brief blithely assumes no need for a basis for state court jurisdiction. *Mathews*, which dealt with the procedures that must be employed when a governmental agency is compelled to act, is totally inapposite. In *Mathews* the government interest "in conserving scarce fiscal and administrative resources," *id.* at 348, shaped the nature of the agency proceeding required. The agency's interest in carrying out its statutory mandate to administer the federal program of disability benefits required some action. Kansas has no corresponding interest that could justify *any* action by its courts with regard to the nonresident class members.

lawsuit has been commenced against them in a Kansas state court and that counsel has been appointed on their behalf. Everyone would agree that this procedure could not pass muster under any due process standard if applied to defendants. How then, can it be upheld when used by a volunteer to collectivize the claims of nonresidents and to assert them before an alien tribunal far, far away. The process is not made less offensive by giving the nonresident an opportunity to take affirmative action to avoid the adjudication.[11] The underlying fiction that silence—failing to opt-out—connotes consent simply cannot be constitutionally countenanced.

Allowing notice and representation to serve as a substitute for affiliating circumstances necessarily would undermine *World-Wide Volkswagen Corp. v. Woodson*, 444 U.S. 286 (1980); *Rush v. Savchuck, supra*; *Kulko v. California Superior Court*, 436 U.S. 84 (1978), and *Shaffer v. Heitner, supra*.[12] This is not and cannot be the law. There is no case supporting it. Notice and representation do not address the constitutional concerns implicit in the jurisdictional basis requirement and do not even become relevant until the standards set forth in *International Shoe* and its progeny have been met.[13]

---

[11] According to respondents' approach, Phillips could use the same procedure to initiate a nationwide class action against a class similar to that represented by the respondents in a forum of its choice to establish that the class had no right to interest.

[12] Neither *Hansberry v. Lee*, 311 U.S. 32 (1940), nor *Smith v. Swormstedt*, 57 U.S. (16 How.) 288 (1854), support respondents. Neither case considered when a class action could proceed in state court absent a legitimate state interest. *Hansberry* involved class members who were residents of the forum state and land in the forum state. *Smith v. Swormstedt* concerned an adjudication by an Ohio federal court of rights to property of an Ohio corporation with its principal place of business in Ohio. In both cases, there was a basis for the courts adjudicating the claims.

[13] The respondents shore up their jurisdictional argument by relying on the "common fund" cases. But they cannot point to any "fund" in this case. As petitioner's earlier brief demonstrates, p. 21 n. 18, and respondents fail to challenge, this case involves nothing more than an aggregation of numerous individual contract claims, which offers no basis for asserting jurisdiction when it otherwise would not exist. Although *in rem* jurisdiction may have satisfied the basis requirement in the "common fund" cases when they were decided, today, this type of contact might not be sufficient to satisfy due process. See *Shaffer v. Heitner*, 433 U.S. 186 (1977).

Thus, the question is not merely a choice between two procedures—an opt-in or an opt-out class action—as respondents simplistically suggest. The question is whether a state court can entertain a nationwide class action in the absence of any constitutional basis for binding unaffiliated nonresident class members. Admittedly, this Court's precedents allow a nonresident plaintiff to consent to having her claim litigated in a state's court. *Keeton v. Hustler Magazine, Inc.*, —— U.S. ——, 104 S. Ct. 1473 (1984). But, it would be intolerable if one plaintiff were allowed to bring other nonresidents' claims before a court for adjudication and to bind those nonresidents on the basis of a "Book of the Month Club" type notice.[14] An attempt to bind nonresidents who remain inactive after receiving notice is jurisdiction predicated on nothing more than "unilateral activity" by self-appointed class representatives and their lawyers.[15] This has not been found constitutionally sufficient to bind an otherwise unaffiliated nonresident defendant. *Helicopteros*

---

[14] An opt-in class action would avoid the constitutional question of whether a state can bind nonresidents who remain inactive after a notice is mailed to the nonresident. See Petitioner's Brief, p. 16 n. 13. At the time this action was filed, Oklahoma had an opt-in class action statute. That statute was replaced by an opt-out statute, effective November, 1984. Okla. Stat. tit. 12, § 2023.C.2.

[15] The "half-fiction" underlying the opt-out provision ignores the fact that silence is ambiguous and "can indicate either consent or objection." Kennedy, *Class Actions: The Right To Opt Out*, 25 Ariz. L. Rev. 3, 21 (1983). The advantage named plaintiffs possess under the assumption that silence connotes consent has been seen as "potential windfall leverage." *Id.*

Nacionales de Colombia, S.A. v. Hall, —— U.S. ——, 104 S. Ct. 1868, 1873 (1984). Requiring that unequivocal affirmative action be taken by nonresidents to submit to jurisdiction is not an unreasonable burden in the case of class members who are unaffiliated with the forum.

C. Recognizing That Jurisdictional Limits Are Applicable To Class Actions Will Not Destroy That Procedure

Notwithstanding the rhetorical and somewhat hysterical protestations of the respondents and the Amici supporting them, Phillips never has argued that the class action be abolished and its position would not lead to that. The alternative to this Kansas class action is not, as the respondents assert, either individual actions or 50 separate class actions. The constitutional possibilities include: (1) valid class actions in a handful of states (at most, those in which the gas leases are located) adjudicating the rights of class members affiliated with each of those states; (2) one class action in one forum that possesses a sufficient connection with the litigation under this Court's precedents that would permit the decision of all claims; or (3) adjudicating claims of those people who have a constitutionally significant connection with a forum state as well as the claims of any one else who affirmatively consents to that state's jurisdiction. Phillips' approach only negates a state's ability to adjudicate the claims of nonresident class members who have no nexus with the forum and have not affirmatively consented to participate.

Preventing state judiciaries from officiously intermeddling with the rights of unaffiliated nonresidents and disputes they have no legitimate interest in does not unduly limit the plaintiffs' ability to obtain meaningful redress.[16] Although this may deprive these plaintiffs of

[16] A defendant thus would not be able to "ignore their obligations" to "small claimants." Respondents Brief p. 14. However, a plaintiff's ability to shop for a forum that would expand the defendant's duties under the contract would be restricted.

greater leverage to bring about a favorable result or to increase the size of any attorney fees award, it does not affect any legitimate state interest. Rather, jurisdictional restraints should be seen as properly allocating judicial business among the states in a manner consistent with our federal system. Applying them undoubtedly will free nonresidents from the effects of adverse court decisions by states having no nexus with them and no legitimate interest in deciding their claims.

III. KANSAS CANNOT CONSTITUTIONALLY EXPORT ITS LAW BY APPLYING IT TO THOSE CLAIMS IN THIS CASE THAT HAVE NO RELATION TO KANSAS

The record shows that over 97.3 percent of the class members are nonresidents of Kansas,[17] and less than one quarter of one percent of the leases are located in Kansas, accounting for only .003 percent of the additional royalties. Pet. App. A9. Moreover, respondents' brief makes no attempt to show that there are any contacts that could create significant state interests to justify the application of Kansas law to the nonresidents or the non-Kansas property or contracts. Respondents totally fail to face up to the reality that this "Court has invalidated the choice of law of a State which has had no significant contact or significant aggregation of contacts, creating state interests, with the parties and the occurrence or transaction." *Allstate Ins. Co. v. Hague*, 449 U.S. 302, 308 (1981).

A. Kansas Law Is Inconsistent With Other Interested States' Law And Its Application To Phillips Was "Arbitrary" And "Fundamentally Unfair"

Instead of attempting to satisfy the prescribed tests for a constitutional choice of substantive law, the respondents argue that the Kansas law applied was of such

[17] The only dispute seems to be whether Kansas residents constitute 2.7 percent of the class (553 members), see Pet. App. A64, or 3.5 percent (1,000 members). See Respondent's Brief, p. 3.

transcendental fairness that the result should not be upset. Whether Kansas law has produced a result that the respondents deem "fair" is beside the point. The question before the Court is whether the Kansas court's choice of law was constitutional. Cf. *Allstate Ins. Co. v. Hague*, at 306 n.6. Moreover, the respondents' frequent references to generally accepted legal principles should not obscure the fact that the court below applied Kansas law to transactions that did not have the slightest relationship to Kansas.

Respondents argue that there are no conflicts between the result reached by the application of Kansas law and the results under other states' laws. This is absolutely wrong. Conflicts exist in at least three areas: (1) the court below held that certain transactions gave rise to an interest obligation when other states' law would lead to a contrary result; (2) universal application of the Kansas notion of equity has defeated the countervailing policies of other states; and (3) the use of Kansas law resulted in the exaction of interest at a much higher rate than would have occurred under other states' laws.[18]

1. *Kansas Imposed An Interest Liability On Transactions That Other States Would Hold Gave Rise To No Interest Obligation*

The unfairness of applying Kansas law is typified by the Kansas Supreme Court's treatment of a group of contracts between Phillips and gas producers.[19] The pric-

[18] The different outcomes noted by Phillips in its initial brief (pages 30-33), were summarily dismissed by the respondents as "collateral" and obfuscatory." This unwillingness to acknowledge the reality of differences in state law underscores an inherent problem in attempting to adjudicate individual claims as part of massive class actions—individually defined rights often are subordinated to the pressure to achieve a global resolution of all claims. The problem is magnified when the class action embraces claims from several states that might define the rights arising from even a single set of facts in substantially different ways.

[19] Phillips is both a producer and purchaser of gas. Phillips creates no new rights in royalty owners simply by purchasing gas

ing provision of these contracts specifically provides that payment of the so-called suspense amounts are not due before the rate increases become final, and that no interest is due on those amounts.[20] These contracts were held by the Kansas Supreme Court to be ineffective to *relieve* Phillips of an obligation to pay interest on "suspended" royalties. Other states in these circumstances would find that no obligation ever arose requiring Phillips to pay interest to royalty owners. The Texas Supreme Court has noted that gas purchase contracts could be written in just the manner these contracts were written to avoid liability for interest to the producer. *Phillips Petroleum Co. v. Stahl Petroleum Co.*, 569 S.W.2d 480, 484 (Tex. 1978). The application of Kansas law to these contracts created a liability that Phillips' contracts expressly negated. The respondents' brief totally fails to address the fact that basic notions of due process and full faith and credit prevent Kansas from invalidating contractual relationships between noncitizens of Kansas about matters having nothing to do with Kansas.

In the same vein, other involved states apparently would not find that Phillips is equitably liable for interest on the large portion of the gas giving rise to the increased royalties that was consumed or otherwise disposed of by Phillips rather than sold to an interstate

from their producer. The gas lease controls the relationship between producer and royalty owner and "operates to divest the lessor [royalty owner] of his right to obtain title in himself by reduction to possession and that thereafter his claim must be based upon the contract with the one to whom he has granted that right." *Greenshields v. Warren Petroleum Corp.*, 248 F.2d 61, 67 (10th Cir. 1957) (applying Oklahoma law). Usually the royalty owner is entitled to receive as royalty a fraction of the gas sale proceeds from the producer. In many cases Phillips agreed with the producer to distribute the royalty portion directly to the royalty owner.

[20] The effect of these contracts was neither raised nor decided in *Shutts I*.

pipeline. Since Phillips did not sell the gas, it never received anyone's "suspense monies." No interest obligation arose because Phillips never acted as a stakeholder and never had the use of any money. Cf. *Phillips Petroleum Co. v. Adams*, 513 F.2d 355 (5th Cir. 1975) (equitable interest allowed for stakeholder's use of money). *Accord*: *First National Bank of Borger v. Phillips Petroleum Co.*, 513 F.2d 371 (5th Cir. 1975); *Phillips Petroleum Co. v. Riverview Gas Compression Co.*, 513 F.2d 374 (5th Cir. 1975).

2. *By Applying Its Own Notions Of "Equity" Kansas Subverted Policies Of Other Interested States*

The national application of the Kansas court's idea of equity ignores the fact that other interested states have chosen to treat these transactions differently. For example, Texas has recognized that any obligation to pay interest is grounded in the contractual relation between Phillips and the payee. *Phillips Petroleum Co. v. Stahl Petroleum Co., supra.* That liability never could be more than a simple debt arising under a contract.

Even if Texas would recognize an equitable basis for an award of interest, it also would recognize countervailing equities. Phillips' offer to all royalty owners to pay additional royalties if those royalty owners agreed to refund any overpayment would stop interest accruing in Texas. *Phillips Petroleum Co. v. Riverview Gas Compression Co.*, 409 F. Supp. 486 (N.D. Tex. 1976). Because the Texas leases account for nearly one-half the money involved in this case, Pet. App. A62, when Kansas ignored this established Texas principle, it increased Phillips' liability dramatically. Phillips has now been held liable for interest on approximately $5.6 million of Texas money, whereas under Texas law it would be liable for interest on approximately $2.0 million. More than doubling its liability in this situation certainly goes well beyond what respondents refer to as "harmless error."

The attempt by the respondents to generalize—indeed, virtually federalize—the basis of the holding below is totally misdirected. The relationship between a royalty owner and a producer has been left to individual state control. *E.g., Mobil Oil Corp. v. Federal Power Commission*, 463 F.2d 256 (D.C. Cir. 1971), *cert. denied*, 406 U.S. 967 (1972). States have been free to regulate this relationship, and have formulated individual policies to address specific problems. The resulting lack of uniformity

> is attributable to our federal system, which leaves to a state, within the limits permitted by the Constitution, the right to pursue local policies diverging from those of its neighbors.

Klaxon Co. v. Stentor Electric Mfg. Co., 313 U.S. 487, 496 (1941). The decision below subverts the ability of the states to take different approaches to the situation presented in this case.

3. *Kansas Applied A Rate Of Interest Substantially Higher Than Those In Force In Other States*

Kansas awarded prejudgment interest at FPC rates that varied between 7 percent and 20.31 percent, largely above 11 percent. Pet. App. A54. These rates were used because the Kansas court deemed that Phillips' corporate obligation to pay interest on refunds at the FPC rate was an express contract providing for an interest rate higher than the Kansas statutory rate. *Herman v. City of Wichita*, 228 Kan. 63, 68, 612 P.2d 588, 593 (1980), *citing*, *Shutts I*, 222 Kan. at 563, 567 P.2d at 1318-19. Other states undoubtedly would assess only a statutory rate of interest. *Phillips Petroleum Co. v. Stahl Petroleum Co., supra.* The effect has been to expose Phillips to a liability of $6.5 million whereas interest at a statutory rate would result in an exposure of $1.9 million.[21] There

[21] The rates prevailing in some other states that are applicable to the present dispute are: Texas—6 percent, Tex. Rev. Civ. Stat. Ann. Art. 5069-1.03 (Vernon); Oklahoma—6 percent, Okla. Const. Art. 14, § 2, Okla. Stat. Ann. tit. 15 § 266; New Mexico—6 percent N.M. Stat. Ann. 56-8-3 (1978).

simply is no basis for believing that Oklahoma, Texas, or any other interested state would abandon their own rule of law in favor of the unique ideas espoused by the court below. Nor is there any constitutional justification for Kansas applying its interest rates to royalties under arrangements having absolutely nothing to do with that state—for example, to Texas gas under a contract between a Texan and Phillips, a Delaware corporation with its principal place of business in Oklahoma.

B. It Is Inappropriate For This Court To Prescribe A Choice Of Law Rule For Kansas

As an alternative to their Kansas-law-is-fair argument, respondents ask this Court to adopt a choice of law rule for Kansas that would apply Oklahoma law to all the transactions aggregated in this class action.[22] This Court should do nothing more than determine that it is constitutionally impermissible to apply Kansas law to the thousands of non-Kansas transactions involved in this lawsuit. It should not render an advisory opinion as to what choice of law rule could be upheld. "It is not this Court's function to establish and impose upon state courts a federal choice of law rule . . . ." *Allstate Ins. Co. v. Hague, supra* at 332 (Stevens, J., concurring). The constitutionality of a choice of law rule looking to Oklahoma law is not before this Court. Since the court below chose to apply Kansas law, "the only question before this Court is whether that choice was constitutional." *Allstate Ins. Co. v. Hague, supra* at 306 n.6.

---

[22] Contrary to respondents' assertions, Phillips does not concede that Oklahoma law could be applicable to all the transactions because most of them do not have sufficient contacts with that state. That is precisely the same reason Phillips believes that Kansas law cannot be applied to all transactions. Moreover, Kansas's demonstrated penchant for favoring royalty owners above all else would not be served by applying Oklahoma law to Kansas residents or transactions.

IV. CONSTITUTIONAL PRINCIPLES OF FEDERALISM REQUIRE SOME RESTRICTIONS ON STATE COURT JURISDICTION AND CHOICE OF LAW

The respondents' brief gives the impression that the only policy objective is how to maximize the utilization of the class action procedure. That is a rather distorted image of the situation. There are much larger questions and values at stake that must be accorded proper weight in order to protect vital elements of our federalism.

Individual states, in deference to the needs of federalism, generally have adopted policies and procedures that respect the interests of the other states. This spirit of cooperation, however, does not assure that conflicts among the states never will arise. States that possess very ardent policies in certain substantive law areas may be more vigorous in their creation, recognition, or enforcement of rights and more willing to perceive wrongs than states that are less strident as to the same matters. A certain amount of discontinuity is inevitable. But when a particular state's zeal becomes excessive and threatens the balance among the states, the conflict becomes intolerable and this Court must act.[23]

In the past, this Court has been successful in minimizing the extent of the conflicts primarily by imposing flexible restrictions on state court jurisdiction. This has been accomplished by demanding a connection among the defendant, the forum, and the litigation, which has required a state to have a legitimate interest in resolving a dispute. The unrestricted use of nationwide class actions based solely on common questions, however, poses a

---

[23] As pointed out by the Amicus, Consumer Coalition, Attorney Generals for eight states submitted an amicus brief in support of the consumers in *Gillette Co. v. Miner*. Contrary to Consumer Coalition's implication, the absence of similar amicus briefs in this case may well signify that the reach of the Kansas courts and the application of Kansas law to the entire class made it unpalatable to support respondents ("the consumers").

serious potential for interstate conflicts, especially in cases like the present one, in which the vast majority of the plaintiffs are nonresidents, their claims have no nexus with the forum, and the forum state attempts to impose its will on the nation by applying its own law. This threat can be minimized by (1) enforcing this Court's statement that "all assertions of state court jurisdiction must be evaluated according to the standard set forth in *International Shoe* and its progeny," and consistently applying the jurisdictional standards enunciated in *World-Wide Volkswagen Corp. v. Woodson, supra, Rush v. Savchuk, supra,* and *Shaffer v. Heitner, supra,* and (2) strictly applying the principle stated in *Allstate Ins. Co. v. Hague, supra,* requiring some state interest exist to justify applying that state's law. Maintaining these standards certainly would diminish the ability to forum shop, as well as the danger that a state, in its ardor to enforce a particular policy, intentionally or unintentionally, will defeat the policy of other states. Cases will be decided less as a result of which forum state is chosen and more in conformity with the policies of those states with legitimate interests in the litigation.

Federalism demands that state judicial power be restrained whenever it intrudes into disputes that properly are left to other states. The exercise of jurisdiction by Kansas in the present case and its parochial application of forum law was an arbitrary extension of its class action procedure to people and transactions that Kansas had absolutely no legitimate interest in affecting and that operated discriminatorily against Phillips and all of the nonresident members of the class. See Brilmayer, *How Contacts Count: Due Process Limitations On State Court Jurisdiction,* 1980 Sup. Ct. Rev. 77, 86. It demonstrates the need for this Court to apply the existing jurisdiction and choice of law standards to protect the legitimate interests of federalism.

CONCLUSION

For the foregoing reasons, the decision of the Court below should be reversed.

Respectfully submitted,

ARTHUR R. MILLER
1545 Massachusetts Avenue
Cambridge, MA 02138

JOSEPH W. KENNEDY
ROBERT W. COYKENDALL
MORRIS, LAING, EVANS, BROCK & KENNEDY, CHARTERED
Fourth Floor, 200 West Douglas
Wichita, KS 67202
316-262-2671

WILLIAM G. PAUL
C. J. ROBERTS
T. L. CUBBAGE, II
Phillips Petroleum Company
Legal Division
1256 Adams Building
Bartlesville, OK 74004

Attorneys for Petitioner